JULY 1988

BUSINESS EVALUATION:

MERGER OF DECISION DATA SERVICE, INC. AND MOMENTUM SERVICE CORPORATION

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Purpose of the Study

Purpose of the Study

Investors in Decision Industries Corporation and Momentum Technologies, Inc. require financial support from the Bank of Boston for a proposed merger of the Customer Service (maintenance) components of the two companies. The Bank of Boston requires a business value assessment and a "Due Diligence" investigation of the planned merged company from an uninvolved, expert third party.

This report combines the results of two recent business valuation studies (i.e., one for Decision Data Service, Inc. and one for Momentum Service Corporation) and then integrates the projected results of the proposed merger strategy to provide a consolidated income and expense and cash flow projection after the merger. This information is then used to determine a value of the merged companies. An assessment of the merger plans is also provided as part of the "Due Diligence" investigation.

Methodology

Methodology

The methodology used for this business value assessment consisted of the following nine major activities:

1. The results of the Case I and Case II income and expense forecast contained in the recent business value assessment of Decision Data Service were used to get an average projected income and expense summary. This was done because the final recommended business valuation in the recent study was based on the average between Case I and II.

2. The results of the average projected income and expense summary for Decision Data Service was then combined with the Momentum Service Corporation Case I income and expense forecast contained in the recent business valuation study of Momentum Service Corporation. Case I was used in setting the final business valuation for Momentum Service Corporation.

3. Two visits were made to Decision Data Service headquarters to interview the key executives selected to manage the merged company. Information was gathered on the merger plans in the following key areas:

   a. Field Organization and Manpower
   b. Information Systems
   c. Marketing/Sales
   d. Parts Logistics/Repair Centers
   e. Compensation and Benefits
   f. Real Estate
   g. Training
   h. Contracts/Offerings
   i. Technical Support
   j. Headquarters Organization and Manpower

4. An estimate was prepared of the reduced spare parts purchases and reduced parts depreciation expense resulting from the merger.

5. A manpower dynamics projection was prepared based on the merger plans and strategies of the key executives. This information provided insight into the savings and costs of the merger as well as future potential savings.

6. An estimate of the impact of the merger on income and expenses was prepared for each major expense category.

7. A consolidated I & E forecast was prepared including the impact of the merger.

8. A cash flow and present value analysis was prepared.

9. A written summation of findings (contained herein) was prepared, along with a recommended valuation based on explicit factors.

Overview of Merger Plans

Overview of Merger Plans

The key executives selected to manage the merged company are primarily from Decision Data Service. As a result the merger plans that have been developed are based primarily on the Decision Data model.

Decision Data Service utilizes a decentralized management approach. Strong measurements and incentives are in place to ensure that each area office (i.e., branch) is motivated to operate on a businesslike basis. Sales responsibility is delegated to these area managers with only support from the headquarters marketing staff. Responsibility for dispatching and credit and collections is also placed at either the area or district level.

Momentum, on the other hand, has more centralized management systems in place, with those responsible for dispatching, credit and collections, and sales reporting to headquarters management.

The highlights of the merger plans in each key area are as follows:

1. Field Organization

The field will be organized into 54 geographic areas and 11 geographic districts. A strong focus will be placed on a decentralized management system with emphasis on sales, profit and loss, customer satisfaction, accounts receivable, dispatching, and technical support.

A significant amount of training will be required to make each area self-sufficient. As a result very few field engineers will be released immediately after the merger. INPUT believes that this training will take about a year to complete, and after that time, some reduction in field engineers could be expected.

Additional people will be added to the merged field organization to support the decentralized management approach in the following categories:

Field Parts Inventory Coordinators	19
Field Administration	25
District Technical Specialists	7

Reduction in field manpower is planned in the following categories:

Field Engineers	6
Area Territory Supervisors	7
District Service Managers	9
Area and Other Service Managers	3

2. Marketing/Sales

The marketing strategy is to do the following:

- Market and sell using local campaigns led by the area service managers.
- Support the area managers with marketing/sales expertise from a small headquarters staff.
- Develop new marketing opportunities through acquisitions and then understand the market before expanding.

As a result of implementing the above strategy in the merged company, there will be a net reduction of 24 people in the marketing and sales organization, which now totals 47 people. Almost all of these people will come from the Momentum organization in Morris Plains and Herkimer or the field marketing representatives.

3. Logistics and Repair

Parts logistics and repair at Momentum Service Corporation is handled by two major centers, one in Herkimer, New York and one in Fremont, California. These centers and the field organization are supported by a national parts information system that carries the location and inventory of all parts and incorporates the ability to place orders on a real-time basis.

Decision Data Service has one major center located in Horsham, Pennsylvania, which is supported by a similar information system.

The merger plan is to close the Herkimer center and consolidate all parts logistics and repair in Horsham and Fremont. There are presently 248 people in the parts logistics and repair function. The merger plan will reduce this to 171—a net decrease of 77 people.

4. Headquarters Administration

At the present time there are 99 people in the headquarters functions of accounting, payroll, billing, accounts receivable, tax, human resources, legal, MIS, etc.

These staffs are presently located in Herkimer, Morris Plains, and Horsham. The merger plan is to consolidate these functions in Horsham with the resulting net reduction of 44 people.

Financial Projections

Financial Projections

Table 1 displays an Income and Expense forecast for Decision Data Service. This forecast is the average between the Case I and Case II forecasts provided in the recent business evaluation study. This average was selected because it was the basis for the final valuation of Decision Data Service.

TABLE 1

DDS & JBS I & E FORECAST
AVERAGE CASE I & II
$ THOUSANDS

	1988	1989	1990	1991	1992	1993
REVENUES						
DDS 14.2%/YR	54,690	62,456	71,325	81,453	93,019	106,228
JBS 22.3%/YR	5,990	7,326	8,959	10,957	13,401	16,389
TOTAL	60,680	69,782	80,284	92,410	106,420	122,617
COST OF SALES						
DDS 86.7% REV	47,394	54,124	61,810	70,587	80,610	92,057
JBS 71.1% REV	4,259	5,209	6,370	7,791	9,528	11,653
TOTAL	51,653	59,333	68,180	78,378	90,138	103,710
GROSS MARGIN						
DDS	7,296	8,332	9,515	10,866	12,409	14,171
JBS	1,731	2,117	2,589	3,167	3,873	4,736
TOTAL	9,027	10,449	12,104	14,032	16,282	18,907
PERCENT REVENUE	14.9	15.0	15.1	15.2	15.3	15.4
SELLING AND G&A						
DDS 6.8% REV	3,717	4,245	4,847	5,536	6,322	7,219
JBS 21.9% REV	1,312	1,604	1,962	2,400	2,935	3,589
TOTAL	5,029	5,849	6,809	7,935	9,256	10,808
I/C CHARGE 1% REV	607	698	803	924	1,064	1,226
NET BEFORE TAX	3,391	3,902	4,492	5,173	5,961	6,873
ESTIMATED TAX 41%	1,390	1,600	1,842	2,121	2,444	2,818
NET AFTER TAX	2,001	2,302	2,650	3,052	3,517	4,055

Table 2 displays the Case I income and expense forecast for Momentum Service Corporation. This was the case used in the final valuation.

TABLE 2

MSC I & E FORECAST
CASE I
$ THOUSANDS

	1988	1989	1990	1991	1992	1993
REVENUES						
PARTS/REPAIRS	1,610	1,430	1,263	1,088	913	738
BASE MAINTENANCE	50,843	43,055	35,403	27,750	20,098	2,445
TPM MAINTENANCE	9,157	16,945	24,597	32,250	39,902	47,555
TOTAL	61,610	61,430	61,263	61,088	60,913	60,738
DIRECT COSTS						
PARTS/REPAIR @ .26	419	372	328	283	237	192
PARTS DEPRECIATION	4,332	5,480	6,560	6,864	5,310	5,576
OTHER DIRECT BASE	29,743	25,187	20,711	16,234	11,757	7,280
PERCENT OTHER DIRECT BAS	58.5	58.5	58.5	58.5	58.5	58.5
OTHER DIRECT TPM	7,390	13,675	19,850	26,026	32,201	38,377
PERCENT OTHER DIRECT TPM	80.7	80.7	80.7	80.7	80.7	80.7
TOTAL DIRECT COSTS	41,883	44,714	47,449	49,406	49,506	51,425
GROSS MARGIN	19,727	16,716	13,814	11,682	11,407	9,313
PERCENT GROSS MARGIN	32.0	27.2	22.5	19.1	18.7	15.3
OPERATING EXPENSES						
QTL ROYALTIES 7.3%	3,712	3,143	2,584	2,026	1,467	908
MKTG/G&A 9.4% REV	5,791	5,774	5,759	5,742	5,726	5,709
TOTAL OPER. EXPENS	9,503	8,917	8,343	7,768	7,193	6,618
PERCENT REVENUE	15.4	14.5	13.6	12.7	11.8	10.9
GROSS OPER. PROFIT	10,224	7,799	5,471	3,914	4,214	2,695
PERCENT PROFIT	16.6	12.7	8.9	6.4	6.9	4.4
OTHER EXPENSE						
MT INTANGIBLE AMOR	2,820	2,820	2,820	1,840	0	0
OTHER	(157)	0	0	0	0	0
TOTAL OTHER	2,663	2,820	2,820	1,840	0	0
INCOME(LOSS) B TAX	7,561	4,979	2,651	2,074	4,214	2,695
PERCENT NET BEFORE TAX	12.3	8.1	4.3	3.4	6.9	4.4
ESTIMATED TAX 41%	3,100	2,041	1,087	850	1,728	1,105
NET AFTER TAX	4,461	2,938	1,564	1,223	2,486	1,590

NOTE: MDS ROYALTIES AND INTEREST EXPENSE ARE NOT INCLUDED.

Table 3 is a consolidation of table 1 and table 2. It therefore represents the income and expense projections before the costs and the savings of the proposed merger have been included.

TABLE 3

CONSOLIDATED I & E FORECAST
DDSI & MSC
$ THOUSANDS

	1988	1989	1990	1991	1992	1993
REVENUES						
DDS 14.2%/YR	54,690	62,456	71,325	81,453	93,019	106,228
JBS 22.3%/YR	5,990	7,326	8,959	10,957	13,401	16,389
MSC CASE I	61,610	61,430	61,263	61,088	60,913	60,738
TOTAL	122,290	131,212	141,547	153,498	167,333	183,355
COST OF SALES						
DDS 86.7% REV	47,394	54,124	61,810	70,587	80,610	92,057
JBS 71.1% REV	4,259	5,209	6,370	7,791	9,528	11,653
MSC TABLE 2	41,883	44,714	47,449	49,406	49,506	51,425
TOTAL	93,536	104,047	115,629	127,784	139,644	155,135
GROSS MARGIN						
DDS	7,296	8,332	9,515	10,866	12,409	14,171
JBS	1,731	2,117	2,589	3,167	3,873	4,736
MSC	19,727	16,716	13,814	11,682	11,407	9,313
TOTAL	28,754	27,165	25,918	25,714	27,689	28,220
PERCENT REVENUE	23.5	20.7	18.3	16.8	16.5	15.4
SELLING AND G&A						
DDS 6.8% REV	3,717	4,245	4,847	5,536	6,322	7,219
JBS 21.9% REV	1,312	1,604	1,962	2,400	2,935	3,589
MSC TABLE 2	9,503	8,917	8,343	7,768	7,193	6,618
TOTAL	14,532	14,766	15,152	15,703	16,449	17,426
DDSI IC CHARGE 1%	607	698	803	924	1,064	1,226
MSC OTHER TABLE 2	2,663	2,820	2,820	1,840	0	0
NET BEFORE TAX	10,952	8,881	7,143	7,247	10,175	9,568
ESTIMATED TAX 41%	4,490	3,641	2,929	2,971	4,172	3,923
NET AFTER TAX	6,462	5,240	4,214	4,276	6,003	5,645

NOTE: MERGER SAVINGS ARE NOT INCLUDED

Both Decision Data Service and Momentum Service provide service in basically the same cities in the United States. The merger therefore presents an opportunity to lower overall costs. In the field major savings are possible in the areas of parts inventory, manpower, and real estate rent.

Table 4 provides a projection of reduced spare parts purchases and the resulting reduction in parts depreciation expense. INPUT believes that a 20% reduction in future parts purchases is a reasonable expectation.

TABLE 4

ESTIMATED PARTS DEPRECIATION SAVINGS
AS A RESULT OF MERGER
$ THOUSANDS

	1988	1989	1990	1991	1992	1993
REVENUE PROJECTION						
DDSI REV(NO JBS)	54,690	62,456	71,325	81,453	93,019	106,228
MSC REV(CASEI)	61,610	61,430	61,263	61,088	60,913	60,738
TOTAL REVENUE	116,300	123,886	132,588	142,541	153,932	166,966
SPARES PURCH. PROJ.						
DDSI	6,808	6,277	6,371	6,225	5,810	5,113
MSC	3,960	5,400	6,000	6,300	6,300	6,000
TOTAL	10,768	11,677	12,371	12,525	12,110	11,113
ASSUMPTION: A 20% REDUCTION IN SPARES PURCHASES AS A RESULT OF THE MERGE						
REDUCED PURCHASES	2,154	2,335	2,474	2,505	2,422	2,223
NET SPARE PURCHASE	8,614	9,342	9,897	10,020	9,688	8,890
PURCHASES AS PERCENT REV	7.4	7.5	7.5	7.0	6.3	5.3
DEPREC. PROJECTION						
DDSI	4,559	5,289	6,037	6,244	6,298	5,959
MSC (CASE I)	4,332	5,480	6,560	6,864	5,310	5,576
TOTAL DEPREC.	8,891	10,769	12,597	13,108	11,608	11,535
REDUCED DEPRECIATION						
YR 1988	431	431	431	431	431	0
YR 1989		468	468	468	468	468
YR 1990			495	495	495	495
YR 1991				501	501	501
YR 1992					484	484
YR 1993						445
TOTAL REDUCTION	431	899	1,394	1,895	2,379	2,393
NET MERGED DEPREC.	8,460	9,870	11,203	11,213	9,229	9,142

Table 5 displays the manpower dynamics planned by management as a result of the merger. Both the field and the nonfield manpower are included in this table.

TABLE 5

MANPOWER DYNAMICS AS RESULT OF MERGER

	Starting Manpower DDSI	Starting Manpower MSC	Total Starting Manpower	Planned Merged Manpower	Delta Manpower
FIELD ENGINEERS	325	324	649	643	(6)
AREA TERR. SUPV.	29	66	95	48	(47)
FIELD INV. COORD.	23	3	26	45	19
DIST. TECH. SPEC.	11	11	22	29	7
TOTAL DIRECTS	388	404	792	765	(27)
DISTRICT SERVICE MGR	8	12	20	11	(9)
DISTRICT ADMIN. MGRS	8	0	8	11	3
AREA SERVICE MGRS	30	26	56	55	(1)
FIELD ADMINISTRATORS	38	14	52	71	19
CREDIT & COLLECTION	8	0	8	11	3
OTHER FIELD EXEC.	3	6	9	7	(2)
TOTAL	95	58	153	166	13
TOTAL FIELD	483	462	945	931	(14)
LOGISTICS	86	162	248	171	(77)
TECH. SUPPORT	43	54	97	58	(39)
MARKETING/SALES	15	32	47	23	(24)
G & A	36	63	99	55	(44)
TOTAL NON FIELD	180	311	491	307	(184)
TOTAL	663	773	1,436	1,238	(198)

Table 6 displays the expected financial impact of the merger on expense projections.

TABLE 6

ESTIMATED IMPACT OF MERGER ON I & E COSTS AND (SAVINGS) $ THOUSANDS

	1988	1989	1990	1991	1992	1993
DIRECT COSTS						
FIELD MANPOWER	(585)	(1,170)	(1,170)	(1,170)	(1,170)	(1,170)
LONG TERM FLD MP	0	(1,142)	(2,284)	(2,284)	(2,284)	(2,284)
REGIONS	(150)	(304)	(304)	(304)	(304)	(304)
ACCT. OPERATIONS	(31)	(62)	(62)	(62)	(62)	(62)
TECH. OPERATIONS	(288)	(576)	(576)	(576)	(576)	(576)
DISPATCH	(170)	(340)	(340)	(340)	(340)	(340)
FREMONT REPAIR C	(724)	(1,449)	(1,449)	(1,449)	(1,449)	(1,449)
HERKIMER REP CTR	(756)	(1,513)	(1,513)	(1,513)	(1,513)	(1,513)
REAL ESTATE RENT	(86)	(502)	(900)	(900)	(900)	(900)
ADDIT. TRAINING	150	150	0	0	0	0
PARTS DEPRECIA	(431)	(899)	(1,394)	(1,895)	(2,379)	(2,393)
TOTAL DIRECT	(3,071)	(7,807)	(9,992)	(10,493)	(10,977)	(10,991)
OPERATING EXPENSE						
MARKETING/SALES	(866)	(1,733)	(1,733)	(1,733)	(1,733)	(1,733)
G & A	(664)	(1,329)	(1,329)	(1,329)	(1,329)	(1,329)
TOTAL OPER. EXP.	(1,530)	(3,062)	(3,062)	(3,062)	(3,062)	(3,062)
TOTAL REDUCTION	(4,601)	(10,869)	(13,054)	(13,555)	(14,039)	(14,053)

Salaries and fringe projections are based on the actual salaries of the people involved in all cases except the long-term field manpower savings.

As stated earlier in this report, INPUT believes that after cross-training is completed (in one year after the merger), a reduction in field engineers will be possible. The savings for long-term field manpower represents an estimated reduction of 54 field engineers beginning in July of 1989.

Dispatch savings are $200,000 per year below those projected by management because INPUT expects that telephone savings will be offset by additional costs of moving to a decentralized system.

The real estate savings are based on a location-by-location analysis and a detailed plan to buy out or cancel certain leases. The buyouts have been netted against the savings and therefore the first two years' savings are smaller than in future years.

Additional training is estimated at $300,000, which is above management's estimate of $186,000. Management plans to do most of the training with existing video cassette courses and thereby eliminate the need to pay travel and living expenses for classroom courses.

The operating expense reductions for marketing and G & A are projected on the basis of the payroll, fringes, and operating expenses of the actual people involved.

Table 7 incorporates the costs and savings into the consolidated income and expense projection and it provides a projection of net after-tax income.

TABLE 7

CONSOLIDATED I & E FORECAST
MERGER SAVINGS INCLUDED
$ THOUSANDS

	1988	1989	1990	1991	1992	1993
REVENUES						
DDS 14.2%/YR	54,690	62,456	71,325	81,453	93,019	106,228
JBS 22.3%/YR	5,990	7,326	8,959	10,957	13,401	16,389
MSC CASE I	61,610	61,430	61,263	61,088	60,913	60,738
TOTAL	122,290	131,212	141,547	153,498	167,333	183,355
COST OF SALES						
DDS 86.7% REV	47,394	54,124	61,810	70,587	80,610	92,057
BS 71.1% REV	4,259	5,209	6,370	7,791	9,528	11,653
MSC TABLE 2	41,883	44,714	47,449	49,406	49,506	51,425
MERGER SAVINGS	(3,071)	(7,807)	(9,992)	(10,493)	(10,977)	(10,991)
TOTAL	90,465	96,240	105,637	117,291	128,667	144,144
GROSS MARGIN	31,825	34,972	35,910	36,207	38,666	39,211
PERCENT REVENUE	26.0	26.7	25.4	23.6	23.1	21.4
SELLING AND G&A						
DDS 6.8% REV	3,717	4,245	4,847	5,536	6,322	7,219
JBS 71.9% REV	1,312	1,604	1,962	2,400	2,935	3,589
MSC TABLE 2	9,503	8,917	8,343	7,768	7,193	6,618
MERGER SAVINGS	(1,530)	(3,062)	(3,062)	(3,062)	(3,062)	(3,062)
TOTAL	13,002	11,704	12,090	12,641	13,387	14,364
DDSI IC CHARGE 1%	607	698	803	924	1,064	1,226
MSC OTHER TABLE 2	2,663	2,820	2,820	1,840	0	0
NET BEFORE TAX	15,553	19,750	20,197	20,802	24,214	23,621
ESTIMATED TAX 41%	6,377	8,098	8,281	8,529	9,928	9,684
NET AFTER TAX	9,177	11,653	11,916	12,273	14,286	13,936
PERCENT REVENUE	7.5	8.9	8.4	8.0	8.5	7.6

Table 8 displays the cash flow projection and the present value of the cash flow for the merged corporation.

TABLE 8

PRESENT VALUE ANALYSIS
AFTER MERGER
$ THOUSANDS

	YEAR 1	YEAR 2	YEAR 3	YEAR 4	YEAR 5	YEAR 6
INCOME AFTER TAX	9,177	11,653	11,916	12,273	14,286	13,936
ADD DEPRECIATION	8,460	9,870	11,203	11,213	9,229	9,142
ADD INTANGIBLE AMORT	2,820	2,820	2,820	1,840		
TOTAL FR. OPERATIONS	20,457	24,343	25,939	25,326	23,515	23,078
SPARES PURCHASES	8,614	9,342	9,897	10,020	9,688	8,890
SURPLUS(DEFICIT)	11,843	15,001	16,042	15,306	13,827	14,188
CUMULATIVE CASH FLOW	11,843	26,844	42,886	58,192	72,019	86,207

DISCOUNT RATE: 9.75%

PRESENT VALUE 62,732

NOTE: THE POTENTIAL EXISTS FOR ADDITIONAL DEPRECIATION AND INTANGIBLE AMORTIZATION BASED ON THE FINAL PURCHASE PRICE AND THE REEVALUATION OF THE DECISION DATA SERVICE PARTS INVENTORY. THIS WOULD INCREASE THE PROJECTED CASH FLOW AND PRESENT VALUE.

It is important to note that the income and expense projections and the cash flow projections do not include severance and benefit payments for the people who will be terminated from employment. These payments are estimated to be $2,600,000.

Recommended Valuation

Recommended Valuation

In reaching a judgement on the recommended valuation for the merged corporation, INPUT believes that consideration must be given to the business mix of products supported by the combined firm.

For example, in the recent valuation of Decision Data Service, INPUT concluded that a price/earning ratio of 24 was justified (i.e., similar for MAI/Basic Four) because a high percentage of its service would still be supporting the hardware products of Decision Industries Corporation. In the case of Momentum Service Corporation a lower price/earning ratio of 13.6 was used (i.e., similar to that of Interlogic Trace).

INPUT believes that because the combined firm has a much smaller percent of the total business supporting the parent company hardware product, a price/earnings ratio of 13.6 is a more reasonable expectation for residual-value purposes.

INPUT believes that the value should be established by adding the present value to the expected residual value at the end of 1993.

Assuming a 13.6 price/earnings ratio in 1993, the residual value would be as follows:

1993—13.6 (P/E Ratio) x $13,936 (1993 Earnings) = 189,529,000

1993—13.6 (P/E Ratio) x $13,936 (1993 Earnings) = $189,529,000
Discounted @ 9.75% to present = $108,464,000

The resulting total valuation under this approach would be as follows:

Present Value	$62,732,000	(From Table 8)
Discounted Residual Value	$108.464.000	
	$171,196,000	

The valuations contained in this report represent INPUT's best efforts based upon information available to INPUT. INPUT has relied upon the accuracy of this information in making its evaluation, and has attempted to verify the information where practical and possible. INPUT does not warrant the accuracy of this information, however, and inaccuracy of information could affect the conclusions reached in this report.